



Senate

General Assembly

File No. 61

January Session, 2011

Substitute Senate Bill No. 899

Senate, March 14, 2011

The Committee on Commerce reported through SEN. LEBEAU of the 3rd Dist., Chairperson of the Committee on the part of the Senate, that the substitute bill ought to pass.

***AN ACT CONCERNING THE USE OF RESEARCH AND
DEVELOPMENT TAX CREDITS FOR PROJECTS IN ENTERPRISE
ZONES.***

Be it enacted by the Senate and House of Representatives in General Assembly convened:

- 1 Section 1. (NEW) (*Effective July 1, 2011*) (a) As used in this section:
- 2 (1) "Commissioner" means the Commissioner of Economic and
3 Community Development;
- 4 (2) "Department" means the Department of Economic and
5 Community Development;
- 6 (3) "Eligible corporation" means any corporation with research and
7 development credits;
- 8 (4) "Eligible development company" means any partnership,
9 including a limited partnership, a limited liability company or any
10 other entity that is treated as a partnership for federal income tax
11 purposes, that (A) is formed by at least one or more eligible

12 corporations and any number of other persons for purposes of
13 conducting a qualified development project described in subsection (c)
14 of this section, and (B) has received a certificate of eligibility from the
15 commissioner, as provided in subsection (b) of this section;

16 (5) "Enterprise zone" means any such zone designated pursuant to
17 section 32-70 of the general statutes; and

18 (6) "Research and development credits" means the tax credits
19 allowed pursuant to section 12-217j or 12-217n of the general statutes.

20 (b) The commissioner may issue a certificate of eligibility to a
21 development company, allowing it to accept research and
22 development credits in furtherance of a qualified development project,
23 as described in subsection (c) of this section. Such eligible development
24 company may receive not more than one certificate of eligibility in any
25 income year. No certificate of eligibility shall be issued after December
26 31, 2020.

27 (c) (1) A qualified development project eligible for the transfer of
28 research and development credits pursuant to this section shall be any
29 commercial or residential real estate development project that is (A)
30 newly constructed or undergoing major expansion or renovation, as
31 determined by the commissioner, (B) located in an enterprise zone, (C)
32 undertaken by an eligible development company, and (D) in
33 compliance with section 31-53 of the general statutes, including any
34 such project that would otherwise be exempt pursuant to the
35 provisions of subsection (h) of section 31-53 of the general statutes.

36 (2) Eligible expenditures for a qualified development project
37 include, but are not limited to, expenditures for (A) land acquisition
38 and permitting, (B) design, (C) construction, (D) demolition, (E)
39 remediation, (F) site preparation and improvements, (G) infrastructure
40 improvements, including, but not limited to, roads, sidewalks, signage
41 or traffic controls, (H) utility improvements for sewer, water, gas,
42 telecommunications, drainage or electricity generation, transmission or
43 distribution, (I) alterations or renovations to any existing structures,

44 including, but not limited to, leasehold improvements and furniture,
45 fixtures and equipment that are necessary or appropriate for use in
46 connection with the qualified development project, (J) tenant
47 procurement, including, but not limited to, marketing, brokerage,
48 rental concessions and moving allowances, and (K) financing or
49 refinancing activities.

50 (3) A qualified development project shall not include any
51 development that is to be used as a facility for any obscene material or
52 performance, as described in section 53a-193 of the general statutes.

53 (d) (1) Notwithstanding the provisions of sections 12-217j and 12-
54 217n of the general statutes, an eligible corporation may (A) contribute
55 research and development credits, in whole or in part, to an eligible
56 development company of which it is a member or partner, which
57 contribution shall not be considered a sale, assignment or transfer for
58 purposes of this section, for use by such eligible development
59 company in furtherance of a qualified development project, or (B) sell,
60 assign or otherwise transfer research and development credits, in
61 whole or in part, to one or more taxpayers, so long as the proceeds
62 from such sale, assignment or transfer are contributed, not later than
63 ninety days after such sale, assignment or transfer, to an eligible
64 development company of which it is a member or partner, for use by
65 such eligible development company in furtherance of a qualified
66 development project.

67 (2) The total amount of research and development credits that may
68 be contributed by an eligible corporation to a particular eligible
69 development company, or sold, assigned or transferred by an eligible
70 corporation to fund a contribution to a particular eligible development
71 company, may not exceed fifty million dollars during any single
72 income year of the eligible corporation.

73 (3) The eligible corporation shall provide to the eligible
74 development company, or to the taxpayer to which such eligible
75 corporation sells, assigns or transfers research and development
76 credits, a schedule showing when each research and development

77 credit contributed or sold, assigned or transferred, is eligible for use by
78 the eligible corporation.

79 (4) An eligible development company that receives research and
80 development credits under subdivision (1) of this subsection may sell,
81 assign or otherwise transfer such credits, in whole or in part, to one or
82 more taxpayers, provided the proceeds from such sale, assignment or
83 transfer are used by such eligible development company exclusively in
84 furtherance of the qualified development project.

85 (e) If an eligible corporation or eligible development company sells,
86 assigns or otherwise transfers research and development credits to
87 another taxpayer, the transferor and transferee shall jointly submit
88 written notification of such transfer to the department not later than
89 thirty days after the date of such transfer. The notification shall include
90 the number of the certificate of eligibility, the date of transfer, the
91 amount of such credits transferred, the tax identification numbers for
92 both the transferor and the transferee, and any other information
93 required by the department. Failure to comply with this subsection
94 shall result in a disallowance of the tax credit until there is full
95 compliance on both the part of the transferor and the transferee.
96 Promptly after receipt of such notification, the department shall issue a
97 tax credit voucher to the transferee. The department shall provide a
98 copy of the notification of assignment and the tax credit voucher to the
99 Department of Revenue Services upon request.

100 (f) Any transferee of any research and development credits may use
101 such credits as a credit against the tax imposed under chapter 207, 208,
102 219 or 229 of the general statutes for any income year in which the
103 eligible corporation would have been eligible to claim such credit. Any
104 transferee of any such credits may sell, assign or otherwise transfer
105 such credits, in whole or in part, to one or more taxpayers. The
106 department shall be notified of any such transfer in the manner
107 provided in subsection (e) of this section, and shall issue a tax credit
108 voucher to any such subsequent transferee, with appropriate
109 adjustments to any prior tax credit vouchers issued.

110 (g) Not later than forty-eight months after the issuance of a
111 certificate of eligibility pursuant to subsection (b) of this section, the
112 eligible development company shall submit an independent
113 certification to the commissioner that the proceeds from the
114 contribution, sale, assignment or transfer of the research and
115 development credits have been used exclusively in furtherance of a
116 qualified development project.

117 (h) In the event of the termination, for any reason, of a qualified
118 development project prior to the expenditure of the entire amount of
119 the net proceeds of the research and development credits contributed,
120 sold, assigned or transferred pursuant to this section, the eligible
121 development company shall pay to the commissioner an amount equal
122 to one hundred per cent of the net unexpended proceeds prior to
123 making any distribution of such proceeds to any eligible corporation
124 or corporations.

125 (i) In the event that, at any time after the issuance of a certificate of
126 eligibility or tax credit voucher, the Department of Economic and
127 Community Development or the Department of Revenue Services
128 determines that there was a material misrepresentation or fraud on the
129 part of any person in connection with the submission of an application
130 to obtain such certificate of eligibility or tax credit voucher, and the
131 result of such material misrepresentation or fraud was that such
132 certificate of eligibility or tax credit voucher was issued, the sole and
133 exclusive remedy of the Department of Economic and Community
134 Development and the Department of Revenue Services shall be to seek
135 redress from the person that committed the fraud or
136 misrepresentation, not from any transferee of the research and
137 development credits.

138 (j) The Department of Economic and Community Development, in
139 consultation with the Department of Revenue Services, shall adopt
140 regulations in accordance with the provisions of chapter 54 of the
141 general statutes, to carry out the purposes of this section.

This act shall take effect as follows and shall amend the following sections:

Section 1	<i>July 1, 2011</i>	New section
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Statement of Legislative Commissioners:

Changed a reference in subsection (c)(1) for accuracy.

CE *Joint Favorable Subst.-LCO*

The following Fiscal Impact Statement and Bill Analysis are prepared for the benefit of the members of the General Assembly, solely for purposes of information, summarization and explanation and do not represent the intent of the General Assembly or either chamber thereof for any purpose. In general, fiscal impacts are based upon a variety of informational sources, including the analyst's professional knowledge. Whenever applicable, agency data is consulted as part of the analysis, however final products do not necessarily reflect an assessment from any specific department.

OFA Fiscal Note

State Impact:

Agency Affected	Fund-Effect	FY 12 \$	FY 13 \$
Department of Economic & Community Development	GF - Cost	66,608	66,608
Comptroller Misc. Accounts (Fringe Benefits) ¹	GF - Cost	15,826	15,826
Department of Revenue Services	GF - Cost	100,000	None
Department of Revenue Services	GF - Potential Revenue Loss	30.0 million - 40.0 million	30.0 million - 40.0 million

Note: GF=General Fund

Municipal Impact: None

Explanation

The bill is estimated to result in a potential revenue loss of between \$30.0 million and \$40.0 million annually from FY 12 to FY 21 (the year in which the program is due to sunset) to the Corporation Business Tax, Insurance Premiums Tax, Personal Income Tax, and Sales and Use Tax. This estimate is based on credits awarded from 2002 to 2010 under the Urban and Industrial Site Reinvestment tax credit, under which an average of \$34.1 million in annual tax credits have been issued. The actual amount of revenue loss is contingent upon eligible development projects being undertaken in one of the 17 designated enterprise zones throughout the state.

¹ The fringe benefit costs for state employees are budgeted centrally in the Miscellaneous Accounts administered by the Comptroller on an actual cost basis. The following is provided for estimated costs associated with changes in personnel. The estimated non-pension fringe benefit rate as a percentage of payroll is 23.76%. Fringe benefit costs for new positions do not initially include pension costs as the state's pension contribution is based upon the 6/30/10 actuarial valuation for the State Employees Retirement System (SERS) which certifies the contribution for FY 12 and

The bill also results in a cost of approximately \$100,000 in FY 12 to the Department of Revenue Services (DRS) associated with changes to the agency's Integrated Tax Administration System (ITAS) and the Taxpayer Service Center (TSC).

Additionally, it is anticipated that the Department of Economic and Community Development will require one economic and community development agent (AR-25) at a cost of \$82,434 (\$66,608 for salary and \$15,826 for fringes) to administer the tax credits.

BACKGROUND

There are approximately \$1.5 billion in unused research and development (R & D) tax credits currently held by corporations; approximately \$25.3 million in R & D credits were claimed in income year 2008, and an additional \$8.9 million were sold in FY 10.

The Out Years

The annualized cost and revenue loss identified above would continue through FY 21, when the program is due to sunset.

FY 13. Therefore, new positions will not impact the state's pension contribution until FY 14 after the next scheduled certification on 6/30/2012.

OLR Bill Analysis**sSB 899*****AN ACT CONCERNING THE USE OF RESEARCH AND DEVELOPMENT TAX CREDITS FOR PROJECTS IN ENTERPRISE ZONES.*****SUMMARY:**

This bill establishes a mechanism by which corporations with unused research and development (R&D) tax credits can sell or otherwise transfer them to a partnership they form to fund commercial or residential projects in one of the 17 state-designated enterprise zones. It specifies the project eligibility criteria and expenditures permitted under the transaction.

Under the bill, the corporation can (1) contribute the credits to the partnership, which can then use them for a development project or transfer them to another taxpayer or (2) directly transfer the credits to another taxpayer. The taxpayer can then use the credits against its corporation business, insurance, sales and use, or personal income taxes or sell the credits to another taxpayer. If the corporation or the partnership sells the credits, the proceeds of any credit transfer must be used for the development project.

To be eligible, the corporation must form a partnership with one or more persons, and the partnership must obtain an eligibility certificate from the Department of Economic and Community Development (DECD). DECD cannot grant certificates after December 31, 2020. DECD, in consultation with the Department of Revenue Services (DRS), must adopt implementing regulations. The bill specifies conditions under which DECD can recapture credits and the parties from whom it and DRS can seek redress in cases of fraud or material misrepresentation.

EFFECTIVE DATE: July 1, 2011

ELIGIBILITY CRITERIA AND EXPENDITURES

The bill allows the DECD commissioner to issue a certificate of eligibility to a development company for a qualified development project. To be eligible, the development company must be a partnership between a corporation with R&D credits issued under CGS §§ 12-217j or 12-217n (see BACKGROUND) and one or more other persons. The partnership must be formed for purposes of conducting a qualified development project as described below. The bill specifies that the partnership can take the form of a limited partnership, limited liability company (LLC), or any other entity that is treated as a partnership for federal income tax purposes.

To be eligible, the development company must also receive a certificate of eligibility from the DECD commissioner. A company can only receive one eligibility certificate in any income year.

To be eligible as a qualified development project, the project must be:

1. a commercial or residential real estate development;
2. newly built or undergoing major expansion or renovation, as determined by the DECD commissioner;
3. in an enterprise zone (see BACKGROUND);
4. undertaken by an eligible development company;
5. in compliance with the prevailing wage laws that apply to public works projects, regardless of cost; and
6. not used as a facility for obscene performances or materials that arouse prurient, shameful, or morbid interests.

The bill specifies a wide range of eligible expenditures for qualified projects. These include expenditures for land acquisition and

permitting; design; construction; demolition; remediation; site preparation and improvements; infrastructure improvements, such as roads, sidewalks, signage, or traffic controls; utility improvements for sewer, water, gas, telecommunications, drainage or electricity generation, transmission, or distribution; alterations or renovations to existing structures, such as leasehold improvements and furniture, fixtures, and equipment necessary or appropriate for use in connection with the project; tenant procurement, including marketing, brokerage, rental concessions, and moving allowances; and financing or refinancing.

Within 48 months following the issuance of a certificate of eligibility, the development company must submit to the DECD commissioner an independent certification that all the proceeds from the transaction have been used to further the qualified project.

MECHANISM FOR CONTRIBUTING OR TRANSFERRING CREDITS

The bill allows corporations with R&D credits to (1) contribute all or part of them to an eligible development company or (2) sell, assign, or transfer all or part of them to other taxpayers so long as it contributes the proceeds to the eligible company within 90 days of receiving them. In either case, the development company must use the credits in furtherance of a qualified project, and the corporation must be a member or partner of the development company receiving the credits.

Development companies receiving credits through these mechanisms may then sell, assign, or transfer all or part of them to other taxpayers, so long as the company uses the sale proceeds solely to further qualified development projects.

The total value of R&D credits that a corporation may contribute or transfer to any one development company through either mechanism is capped at \$50 million a year in each of the corporation's income years. The corporation must provide the eligible company or transferee taxpayer a schedule showing when the corporation can use each R&D credit.

The bill does not cap (1) the total amount of credits a single corporation can contribute or transfer or (2) the aggregate amount of credits that can be contributed or transferred by all corporations in the state.

Under the bill, a transferee of R&D credits may use them as a credit against its corporation business, insurance, sales and use, or personal income taxes for any income year in which the corporation could have claimed the credit. The transferee can also sell or otherwise transfer some or all of the credits to other taxpayers.

NOTICE TO DECD; TAX CREDIT VOUCHERS

If an eligible corporation or development company sells or otherwise transfers R&D credits to another taxpayer, the transferor and transferee must jointly notify DECD, in writing, within 30 days of the transfer. The notification must include the number of the certificate of eligibility, the transfer date, the amount of credits transferred, the parties' tax identification numbers, and any other information DECD requires. The tax credit is disallowed until both the transferor and transferee fully comply with the notice requirement. After receiving the notice, DECD must promptly issue a tax credit voucher to the transferee. Upon request, DECD must provide DRS with a copy of the notification of assignment and the tax credit voucher.

Transferees who sell or otherwise transfer credits to other taxpayers must also notify DECD in the manner described above. DECD must issue tax credit vouchers to subsequent transferees, adjusting for any vouchers issued previously.

RECAPTURE OF UNEXPENDED NET PROCEEDS

If a qualified project ends before an eligible company has spent the entire net proceeds of the R&D credits contributed or transferred as outlined above, the company must pay the DECD commissioner an amount equal to all of the net unexpended proceeds before distributing any such proceeds to eligible corporations.

FRAUD AND MISREPRESENTATION

If DECD or DRS finds anyone has committed material misrepresentation or fraud in connection with a submission of an application for a certificate of eligibility or tax credit voucher, and that the misrepresentation or fraud resulted in the issuance of the certificate or voucher, they can seek redress only from the person that committed the fraud or misrepresentation, and not from any transferee of R&D credits. The bill does not specify what happens if the transferee is responsible for the fraud or misrepresentation.

BACKGROUND

Research and Development Tax Credits (CGS §§ 12-217j and 12-217n)

The R&D tax credits issued under CGS § 12-217j are based on the growth in a corporation's R&D expenditures, while the credits issued under CGS § 12-217n increase with the amount of such expenditures.

The credits can be carried forward. Qualified small businesses—those with gross incomes not exceeding \$70 million in the previous income year—can obtain a refund equal to 65% of their unused credits (CGS § 12-217ee).

Enterprise Zones

There are currently 17 municipalities with enterprise zones: Bridgeport, Bristol, East Hartford, Groton, Hamden, Hartford, Meriden, Middletown, New Britain, New Haven, New London, Norwalk, Norwich, Southington, Stamford, Waterbury, and Windham.

COMMITTEE ACTION

Commerce Committee

Joint Favorable

Yea 17 Nay 0 (02/24/2011)